

# Fiscal Note

**BILL #** HB 2649

**TITLE:** computer data centers; tax incentives

**SPONSOR:** Toma

**STATUS:** House Engrossed

**PREPARED BY:** Hans Olofsson

## Description

HB 2649, as amended by the House Ways and Means Committee, would provide a Transaction Privilege Tax (TPT) exemption under the prime contracting classification for the installation of computer data center equipment at data centers certified by the Arizona Commerce Authority (ACA).

The bill would also amend the current income tax credit for renewable energy investment and production for self-consumption by international operations centers (IOC) by allowing investments in new renewable energy facilities to be made by third-party entities on behalf of or for the direct benefit of the taxpayer.

## Estimated Impact

The bill would result in one-time revenue loss of up to \$(10,000) in FY 2022 for tax refunds. With one exception, we are uncertain whether data centers have paid the prime contracting tax in the past. If they have not paid the contracting tax, the bill would not have an ongoing impact. The Department of Revenue (DOR), however, has recently opined that there is at least one instance where the prime contracting tax was required to be paid. If that decision were more broadly applied by DOR, the bill would result in foregone revenue. Due to a lack of industry-specific data on the cost of installing data center equipment, we cannot determine this potential magnitude.

The change to the income tax credit for renewable energy investment and production for self-consumption by IOCs would have no fiscal impact.

## Analysis

### TPT Contracting Exemption for Data Centers

Under current law, equipment that is purchased and installed at a certified computer data center in Arizona is exempt from retail TPT and Use Tax. This bill would exempt the installation, assembly, repair or maintenance of such equipment from prime contracting TPT if it has "independent functional utility." (Independent functional utility means that the equipment "can independently perform its function without attachment to real property" such as land or a building.)

According to an industry representative, since the inception of ACA's computer data center program in 2013, certified data centers have interpreted existing statute [A.R.S. § 41-1519(O)(14)] to mean that equipment that is exempt from retail TPT and Use Tax is also exempt from prime contracting tax when installed at the data center. According to the same industry representative, this is the reason that certified data centers did not pay prime contracting TPT on the cost of installing equipment until late in 2019 when a contractor informed one of the data centers that their contract for installation was subject to prime contracting TPT.

While we were unable to determine whether prime contracting tax was paid on the installation of the equipment at that data center, we contacted DOR and they confirmed that they were familiar with this case. Moreover, DOR also informed us that they have opined that under their interpretation of statutes, this particular contract was not exempt from prime contracting TPT.

Based on the information above, which we cannot independently confirm, the bill could result in a one-time General Fund revenue loss of up to \$(10,000) in FY 2022 (the maximum statewide aggregate refund amount under the bill).

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The ongoing revenue impact depends on whether the bill is compared to current law or current practice. Relative to current law, the bill would result in a revenue loss since equipment that is installed at data centers would be exempt from prime contracting TPT. Relative to current practice, however, the bill would have no ongoing revenue impact since we understand that no certified data center in Arizona (with the possible exception for the one mentioned above) has paid the prime contracting tax in the past.

As noted above, we cannot independently verify the information provided by the industry representative. Moreover, due to a lack of specific data on the cost of installing data center equipment, we cannot quantify the bill's fiscal impact at the current time.

#### Credit for Renewable Energy Investment and Production for Self-Consumption by IOCs

Current law provides a corporate income tax credit for investment in new renewable energy facilities that produce energy for self-consumption using renewable energy sources if the power is primarily used for an International Operations Center (IOC). The amount of the credit per taxpayer is \$5 million per year for 5 years, for a total of \$25 million. The aggregate credit cap per year is \$10 million. Pursuant to A.R.S. § 43-1164.05(C), an IOC that is initially certified by ACA after December 31, 2018 is not allowed to claim this credit.

According to DOR, only one company was certified as an IOC and qualified for the credit before December 31, 2018. The annual credit cost of this IOC is estimated to be \$5 million, for a total of \$25 million over 5 years. This means that \$5 million of the maximum allowable credit amount of \$10 million per year is used under current law. The changes to credit under bill would not affect any company certified as an IOC after December 31, 2018. For this reason, the changes to the credit under HB 2649 would have no fiscal impact relative to current law.

#### **Local Government Impact**

Under the statutory distribution formula, a certain percentage (based on TPT classification) of state TPT is shared with incorporated cities and towns as well as counties. Therefore, insofar as this bill reduces state TPT, it would also result in reduced revenue distributions to municipalities and counties.

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